# Supreme Court of Kentucky

**CASE NO. 2014-SC-000549**

**KENTUCKY COURT OF APPEALS**
**CASE NO. 2013-CA-000612-MR**

**On Appeal From Franklin Circuit Court**
**Civil Action No. 12-CI-1441**

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SUPREME COURT

COMMONWEALTH OF KENTUCKY,
KENTUCKY DEPARTMENT OF INSURANCE, and
SHARON P. CLARK, in her official capacity as COMMISSIONER,
KENTUCKY DEPARTMENT OF INSURANCE, APPELLANTS

v.

UNITED INSURANCE COMPANY OF AMERICA,
THE RELIABLE LIFE INSURANCE COMPANY,
RESERVE NATIONAL INSURANCE COMPANY APPELLEES

## BRIEF FOR APPELLEES

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## CERTIFICATE OF SERVICE

It is hereby certified that a true and correct copy of this Brief for Appellees was served by U.S. Mail this 11th day of December, 2015, to the following: Samuel Givens, Clerk, Kentucky Court of Appeals, 360 Democrat Dr., Frankfort, KY 40601; Hon. Phillip Shepherd, Judge, Franklin Circuit Court, Franklin County Courthouse, 222 St. Clair St., Frankfort, KY 40601; Hon. Jack Conway, Attorney General, 700 Capitol Avenue, Suite 118, Frankfort, KY 40601; Peter Ervin, Executive Director, Public Protection Cabinet, Office of Legal Services, Capital Plaza Tower, 500 Mero Street, 5th Floor, Frankfort, KY 40601, Counsel for Appellants; Mark D. Overstreet, 421 West Main Street, P.O. Box 634, Frankfort, KY 40602, Counsel for *Amici* The Insurance Institute of Kentucky and The National Alliance of Life Companies.

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## INTRODUCTION

This case involves the interpretation of a statute, the Kentucky Unclaimed Life Insurance Benefits Act, which imposes new escheat, claims-payment, and beneficiary search obligations on insurers. The Court of Appeals properly determined that retroactive enforcement of the Act against Appellees' life insurance policies issued prior to the Act's effective date would violate Kentucky's statutory presumption against retroactive legislation, codified at KRS 446.080(3), because the Act changes Appellees' substantive rights and obligations, and because it does not contain an express statement that the General Assembly intended retroactive enforcement.

## STATEMENT CONCERNING ORAL ARGUMENT

Appellees submit that oral argument would assist the Court in resolving the questions presented in this appeal. These questions are critical to the regulation of insurance in the Commonwealth and involve matters of first impression. The courts below were the first in the country to address whether the novel obligations the Act imposes on insurers can be retroactively enforced without violating either the presumption against retroactive laws or the Contract Clauses of the Kentucky and United States Constitutions. Appellees suggest that oral argument is necessary for full consideration of these important issues.

## COUNTERSTATEMENT OF POINTS AND AUTHORITIES

## COUNTERSTATEMENT OF THE CASE

The Court of Appeals appropriately resolved this case by following a straightforward canon of statutory construction that is "deeply rooted in our jurisprudence" and "centuries older than our Republic." *Landgraf v. USI Film Products*, 511 U.S. 244, 265 (1994). The recently-adopted Unclaimed Life Insurance Benefits Act, KRS 304.15-420 (the "Act") requires insurers—for the first time—to search electronic databases for evidence that their insureds have died, to confirm that evidence, and to take affirmative steps to locate beneficiaries. If these new requirements are enforced retroactively against life insurance policies issued before the Act's effective date, it will eliminate Appellees' express contractual right to require their "receipt" of "due proof of death" from a claimant before taking steps to investigate potential deaths or to pay claims. Separately, retroactive enforcement of the Act will require Appellees to escheat life insurance proceeds to the State earlier than existing law provides.

Kentucky's well-established presumption against retroactive laws, codified in KRS 446.080(3), dictates that the Act does not apply to Appellees' pre-existing contracts because it contains no "express" statement that the General Assembly intended to retroactively impose such changes on these past transactions. Although Appellants argue that the Act is merely remedial and therefore does not fall within the presumption, the Court of Appeals correctly concluded that the Act substantially changes the relationship between Appellees and their policyholders and so cannot be applied retroactively to policies issued before its effective date.

## I. Factual background.

### A. Appellees' contracts with their policyholders.

Appellees United Insurance Company of America, The Reliable Life Insurance Company, and Reserve National Insurance Company ("Appellees") have been licensed to issue life insurance policies in Kentucky for several decades.[1] Together, Appellees have a combined total of over 9,000 life insurance policies in force in the Commonwealth.[2] Appellees' policies generally have lower face amounts, and thus lower premiums, than those offered by many other life insurers.[3]

Appellees' life insurance policies are contracts between Appellees and their policy owners. Among other things, the contracts establish the terms on which the Appellees will pay a claim for benefits. The contracts expressly require the person seeking benefits to initiate the claim process by furnishing Appellees with due proof of the insured person's death. This contractual requirement is consistent with the "traditional" standard that has applied across the life insurance industry for "many years." J. Ebadi, M. Goldman, & S. Schaunaman, *A Tale of Two Standards: Unclaimed Property Upheaval in the Insurance Industry*, 22 J. Multistate Tax & Incentives 1, 24 (Oct. 2014); *see Andrews v. Nationwide Mut. Ins. Co.*, No. 97891, 2012 WL 5289946, at *4 (Ohio Ct. App. Oct. 25, 2012) (Appendix A) (holding that the due proof of death requirement is "standard" nationwide). Indeed, this industry-wide practice reflected in Appellees' policies dates back well over a century. *See, e.g., Cooper v. Bd. of Review of*

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[1] R. 1/16/13 Dep. T. Myers ("Myers Dep."), Ex. 4, Decl. of T. Myers ("Myers Decl.") ¶ 7 (filed 03/19/13); R. 1/14/13 Dep. A. Schallhorn ("Schallhorn Dep."), Ex. 1, Decl. of A. Schallhorn ("Schallhorn Decl.") ¶ 7 (filed 03/19/13).

[2] R. 9, Compl. ¶ 22; Myers Decl. ¶ 8; Schallhorn Dep. at 36:10–20.

[3] Myers Decl. ¶ 5–6; Schallhorn Decl. ¶ 5–6.

*Montgomery Cnty.*, 207 Ill. 472, 475 (1904) (interpreting life insurance policy to require "proof of death as a condition precedent to the payment"); *Da Rin v. Cas. Co. of Am.*, 108 P. 649, 651–52 (Mont. 1910) (same); *Metro. Life Ins. Co. v. Wagner*, 109 S.W. 1120, 1121 (Civ. Ct. App. Tex. 1908) (same).

Appellees make this "due proof of death" requirement clear to their policyholders. Appellees' life insurance policies are concise documents, usually totaling no more than 10 pages.[4] In clear and unambiguous terms, each policy uniformly establishes that Appellees must "receive" "due proof of death" as a condition precedent to their investigation or payment of any claim for benefits. *Id.* The text that imposes this condition typically appears on the very first page of the life insurance policy, in a short and plain statement such as the following:

> "We will pay, upon *receipt of due proof of the death of the Insured*, the sum of the following . . . ."[5]
>
> "We will pay the Death Benefit to the beneficiary when we *receive proof of the Insured's death*."[6]
>
> "Payment will be made *after we receive proof of the Insured's death*, subject to the terms of this policy."[7]

This language makes plain that Appellees have a "passive role" in "establishing an insured party's proof of death." *Andrews*, 2012 WL 5289946, at *4. Appellees' obligation to investigate or pay a claim is triggered only upon their "receipt" of information from the person seeking benefits. Indeed, courts interpreting this standard language consistently have held that "the insurer has *no duty to make an independent*

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[4] *See, e.g.*, R. 346–525.

[5] R. 352, Compl. Exh. 4 at 7 (emphasis added).

[6] R. 480, Compl. Exh. 16 at 1 (emphasis added).

[7] R. 375, Compl. Exh. 7 at 1 (emphasis added).

*investigation* to determine if the beneficiary is entitled to make a claim." 13 L. Russ & T. Segalla, *Couch on Insurance* § 189:78 (3d ed. 2013) (emphasis added); *infra* at 17–18 (collecting additional authorities).

Kentucky's Insurance Code expressly confirms that an insurer's obligation to investigate or pay a claim is triggered only after the insurer is "*furnished*" with "*notice and proof of claim*" from the person seeking benefits. KRS 304.12-235 (emphasis added). This corroborates the insurer's passive role in establishing proof of death: The claimant must "furnish" the information—*i.e.*, "provide or supply what is needed." Webster's Third New Int'l Dictionary 923 (1971).

Consistent with the Kentucky Insurance Code and decades of industry practice, the Kentucky Department of Insurance (the "Department") routinely has approved life insurance policy forms that contain this contractual "due proof of death" requirement, including the forms for *every* policy Appellees have issued in Kentucky.[8] *See* KRS 304.14-120(1) (stating that no "insurance policy" may be issued in the state unless it is set forth on a form "filed with and approved by the commissioner").

This allocation of contractual rights and responsibilities, set forth in Appellees' life insurance polices and approved by the Department, results in the efficient settlement and payment of claims. The beneficiaries of an insured person typically are close family members, and therefore are in the best position to learn of the insured person's death and to notify the insurer of that fact. By placing the obligation to report death on beneficiaries or other claimants, Appellees' life insurance policies assign that responsibility to the individuals with the best access to the necessary information and the

[8] *See* R. 10–11, Compl. ¶¶ 29–30.

greatest incentive to bring it forth. This enhances the probability that claims will be submitted quickly and accurately, and paid out in a prompt and orderly fashion.

**B. The Act imposes new obligations on insurers.**

The Act is based on a 2011 model law drafted by the National Conference of Insurance Legislators ("NCOIL"). To date, nineteen states, including Kentucky, have adopted versions of this model law.[9] Kentucky's Act was adopted in 2012, and became effective on January 1, 2013. KRS 304.15-420.

The Act fundamentally alters the relationship between insurer and policyholder reflected in existing contracts. Under the Act, a life insurer may no longer await "receipt" of "due proof of death" before taking steps to investigate and pay claims. Instead, twice each year, the insurer must search for evidence of death for all of its insureds by comparing its life insurance policies against the Death Master File administered by the Social Security Administration (the "DMF") or an alternative database that is "at least as comprehensive." KRS 304.15-420(2)(b), (3)(a).

If the insurer discovers a match between the name, date of birth, or Social Security number of any of its insureds and an entry in the DMF, the insurer must take a series of additional steps to investigate the match, to locate and assist beneficiaries in making a claim, and to escheat the proceeds to the State if beneficiaries cannot be found. In particular,

- The insurer must, within 90 days of identifying the match, complete "a good faith effort" to "confirm the death," verify that the deceased is among its insureds, and "[d]etermine whether benefits are due." *Id.* 304.15-420(3)(b)(1), (2).

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[9] As discussed below, many of the states that have most recently adopted the law have expressly restricted its retroactive enforcement. *See infra* at 29.

- If death is confirmed and benefits are payable, the insurer must, within the same 90-day window, take steps to "locate the beneficiary" and "[p]rovide . . . claims forms or instructions" to the beneficiary necessary to submit a claim. *Id.*
- If the beneficiary cannot be identified or located, the insurer must escheat the policy proceeds to the Treasurer within three years of confirming the DMF match. *Id.* 304.15-420(5).[10]

The Act's stated purpose is to require "recognition of the escheat statute" and to require "complete and proper disclosure, transparency, and accountability relating to any method of payment for life insurance death benefits." *Id.* 304.15-420(1). Failure to comply with the Act is an "unfair" and "deceptive trade practice" that exposes an insurer to substantial civil and criminal penalties, including the revocation of its license. *Id.* 304.15-420(8); 304.99-010, -020.

**1. The Act's requirements conflict with existing contracts.**

The Act does away with Appellees' contractual right to require "receipt" of "due proof of death" as a condition to their investigation and payment of claims. This deprives Appellees of their bargained-for right to require the person seeking benefits to initiate the claim process. Instead, the Act now requires Appellees to incur all the administrative costs necessary to search for evidence of their insureds' deaths, confirm that evidence, and locate beneficiaries.

None of these costs are anticipated in Appellees' existing contracts. Appellees relied on their contractual right to require the claimant to furnish due proof of death when they established the price of their pre-existing life insurance policies—*i.e.*, the premium the insured must pay in exchange for Appellees' agreement to pay the death benefits. Appellees' premium rates for policies issued prior to the Act's effective date do not

[10] The insurer must also "document" the steps it took to satisfy the foregoing requirements and must file a certification with the State regarding compliance. *Id.* 304.15-420(3)(b).

account for the administrative costs that would be necessary to search the DMF for evidence of death, confirm that evidence, or locate beneficiaries.[11] These costs are significant, *see infra* at 16–17, and the Act specifically denies Appellees any right to offsetting compensation. *Id.* 304.15-420(4). The Act also eliminates Appellees' right to retain and invest policy cash flows by compelling Appellees to pay policy proceeds sooner—*i.e.*, upon their own independent search and confirmation of evidence of death—rather than upon receipt of due proof of death from a claimant. *Id.* 304.15-420(5).

**2. The Act imposes new escheat obligations on Appellees.**

In addition to these requirements, the Act alters the deadline by which insurers must escheat proceeds for unclaimed life insurance policies to the State. Prior to the Act, Kentucky's Unclaimed Property Law required insurers to escheat life insurance proceeds to the Treasurer within three years of either of the following two events: (1) if the insurer received "actual proof of the death," but no beneficiary was available to accept payment, or (2) if the insurer never received proof of death, but the insured person reached the "limiting age" established by State law—*i.e.*, the age at which the insured person is presumed dead. *See* KRS 393.062. The limiting age is set by Department regulations and is incorporated into insurers' policies. 806 KAR 6:010, :060, :075. In Kentucky, the limiting age on most life insurance policies is age 99. *Id.*

The Act expedites this deadline. The Act requires insurers to escheat life insurance policy proceeds to the Treasurer "within three years of a match against the DMF," even if the insurer has not received due proof of death, and even if the insured has not reached the limiting age. KRS 304.15-420(5). Therefore, the Act significantly

[11] Myers Decl. ¶ 12; Schallhorn Dep. ¶ 11.

accelerates the Treasurer's receipt of revenue for unclaimed life insurance policies by many years earlier than existing law provides.

## II. Procedural history.

### A. The Circuit Court proceedings.

Appellees do not dispute the General Assembly's authority to apply the Act to *new* life insurance policies issued after its effective date. Indeed, Appellees are complying with the Act as to new policies. Appellees commenced this action on November 8, 2012 solely to challenge the Act's retroactive enforcement against their *pre-existing* life insurance policies. Appellees sought a declaratory judgment on two limited grounds: First, KRS 446.080(3)'s presumption against retroactivity prohibits the Act from being applied to life insurance policies issued prior to its effective date. Second, and in the alternative, the Act's retroactive enforcement violates the Contract Clauses of the Kentucky and United States Constitutions. Ky. Const. § 19; U.S. Const. art I, § 10.

On April 1, 2012, the Circuit Court issued an order granting summary judgment to the Department. The Circuit Court held that KRS 446.080(3)'s presumption against retroactivity did not apply to the Act because the Act is a "remedial or procedural" statute, not a "substantive" one.[12] In addition, the Circuit Court held that retroactive enforcement of the Act does not violate the Contract Clause because the Act "does not impair" contract rights, including Appellees' contractual rights to require due proof of death.[13] In the alternative, the Circuit Court held that any such impairment was "well

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[12] R. 777–79, Circuit Court Opinion and Order at 6–8.

[13] R. 779, *id.* at 8.

justified" because the "insurance industry" is "highly regulated" and because the life insurance contracts at issue are "unjust."[14]

The Circuit Court issued its ruling just days before the Act required Appellees to perform their first mandatory DMF search. Accordingly, the Circuit Court temporarily stayed the Act's enforcement against Appellees' pre-existing life insurance policies, enabling Appellees to seek a stay pending appeal from the Court of Appeals. The Court of Appeals granted the stay of enforcement, and subsequently considered the merits.[15]

**B. The Court of Appeals proceedings.**

In a unanimous opinion issued on August 15, 2014, the Court of Appeals reversed the Circuit Court's judgment. The Court of Appeals held that KRS 446.080(3)'s presumption against retroactivity applies to the Act because the Act is "substantive," not "remedial." (Opinion at 7–9.) As the Court of Appeals explained, the Act "clearly imposes new and substantive requirements which affect the contractual relationship between insurer and insured." (*Id.*) Specifically, "the insurers' obligations under the contracts arise only upon receipt of notice and due proof of death. However, the Act now requires insurers to actively investigate potential claims and provide notice to beneficiaries *before* any notice or proof of death is provided." (*Id.* at 9 (emphasis added).) Thus, "the Act *shifts the burden* of obtaining evidence of death and locating beneficiaries from the insured's beneficiaries and estate to the insurer." (*Id.* at 10 (emphasis added).) This is "a substantive and not a remedial alteration of the contractual relationship." (*Id.* at 9.)

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[14] R. 780, *id.* at 11.

[15] Court of Appeals Docket Entries ("D.E.") 9 (Apr. 8, 2013); D.E. 13 (Jul. 16, 2013).

Applying KRS 446.080(3)'s presumption, the Court of Appeals concluded that the Act cannot be enforced retroactively because it lacks the "express" statement of retroactive intent required by the presumption. (*Id.* at 7.) In so holding, the Court of Appeals rejected the Department's argument that the Act's oblique reference to "in force policies" could qualify as such an "express" statement of legislative intent that the Act be applied retroactively. (*Id.*) "In the absence of a clearer expression of the General Assembly's intent," the Court of Appeals declined to "presume" that the General Assembly intended to require retroactive enforcement. (*Id.*)

Having resolved the case on these statutory grounds, the Court of Appeals declined to reach the constitutional claims.

### C. The General Assembly amends the Act without addressing retroactivity.

On April 8, 2014—while this matter was pending in the Court of Appeals—the General Assembly amended the Act to require insurers to search the DMF on a semiannual (rather than quarterly) basis, and to make other changes not relevant here. 2014 Ky. Laws Ch. 60 (HB 414). Although this litigation challenging the Act's retroactive enforcement was pending at that time, the General Assembly did not amend the Act to declare its intent regarding whether the Act should apply retroactively to pre-existing life insurance policies.

## SUMMARY OF THE ARGUMENT

The Court of Appeals' ruling should be affirmed. Under KRS 446.080(3)'s well-established presumption against retroactivity, legislation cannot be applied to past transactions without an express statement that the General Assembly intended such an effect. *Commonwealth Dep't of Agric. v. Vinson*, 30 S.W.3d 162, 168 (Ky. 2000). That

presumption applies to all "substantive" laws, as opposed to laws that are merely "procedural or remedial." *Id.* The Court of Appeals properly determined that the Act is "substantive" because the Act imposes payment obligations and administrative costs on insurers that conflict with their contracts. Under the Act, Appellees may no longer rely on their contractual right to condition their investigation and payment of claims upon "receipt" of "due proof of death." Instead, Appellees must adopt a regular program to affirmatively search for evidence of their insureds' deaths, confirm the evidence, and locate beneficiaries before that contractual condition is satisfied. KRS 304.15-420(2)(b), (3)(a), (3)(b). As the Court of Appeals explained, this imposes a "substantive" change on the contracts because it "shifts the burden" of obtaining evidence of death and locating beneficiaries from the claimant to the insurer. (Opinion at 9); *infra* Part I.A.1.

In addition, the Court of Appeals properly held that the Act is substantive for the independent reason that it significantly alters insurers' escheat obligations. This is precisely the same conclusion the Sixth Circuit reached in virtually indistinguishable circumstances in *American Express Travel Related Servs. Co. v. Kentucky*, 730 F.3d 628 (6th Cir. 2013) (Appendix B). As Judge Siler's opinion for the Sixth Circuit in that case makes clear, laws that hasten escheat deadlines are "substantive," not "remedial." *Id.* at 633; *infra* Part I.A.2. According to KRS 446.080(3), these substantive requirements cannot be enforced retroactively because the Act contains no "express" statement that the General Assembly intended it to apply to past transactions. *Infra* Part I.B.

The Court of Appeals decision is a classic exercise in judicial restraint. By deciding this case under the presumption against retroactivity, the Court of Appeals resolved the dispute on the narrowest possible ground, avoiding Appellees' constitutional

challenges to the Act. This is precisely the result KRS 446.080(3) is designed to achieve. It historically has been the legislature's prerogative to decide in the first instance whether the purported "social" advantages of retroactive legislation outweigh the constitutional problems that retroactive enforcement triggers. *Landgraf*, 511 U.S. at 266. The Court of Appeals' decision supports the separation of powers by deferring to the General Assembly on this important question. *Infra* Part I.C.

The Department argues that the presumption against retroactivity should be ignored because the Act "remedies" what the Department perceives as unfair terms in the insurance contracts. (Dep't Br. at 1, 3–4.) But that misstates what constitutes a "remedial" law in the context of the presumption against retroactivity. In that context, a remedial law is one that merely affects the procedure for vindicating a substantive right, without altering the underlying substantive rights or duties themselves. *Infra* at 24–25. It is not a law that "remedies" a perceived societal ill. In sum, in the context of the presumption against retroactivity, remedial legislation must "not impair rights a party possessed when he or she acted or give past conduct or transactions new substantive legal consequences." *Moore v. Stills*, 307 S.W.3d 71, 81 (Ky. 2010). The Act is not merely remedial. It substantively changes Appellees' obligations under the contracts and their escheat deadlines. The Act is therefore controlled by KRS 446.080(3)'s presumption. As a result, the Department's arguments about the purported "social" benefits of the Act's retroactive enforcement are irrelevant as a matter of law. *Infra* Part I.A.3. Those arguments are best directed to the General Assembly, not this Court.

For all these reasons, this Court need not look further than the presumption against retroactivity to decide this case. However, if this Court confronts the

constitutional issues, it is clear under well-established case law that retroactive enforcement of the Act violates the Contract Clause of the Kentucky and United States Constitutions. *Infra* Part II. By shifting the burden to establish proof of death from claimants to insurers, the Act substantially impairs Appellees' contractual right to require the claimant to establish proof of death, on which Appellees relied in setting premiums for their pre-existing life insurance policies. *See Allied Structural Steel v. Spannaus*, 438 U.S. 234 (1978). This impairment is unconstitutional because it is not a "narrow" and "reasonabl[y]" tailored means of achieving a "significant" public purpose. *Id.* at 244, 248–50. The State has multiple alternative tools available to accomplish the Act's purported objectives without violating contract rights.

## ARGUMENT

### I. KRS 446.080(3)'s presumption against retroactivity prevents the Act from being applied to life insurance policies issued prior to its effective date.

KRS 446.080(3) prohibits the Act from being applied to life insurance policies issued prior to its effective date. KRS 446.080(3) provides that "no statute shall be construed to be retroactive, unless expressly so declared." This presumption applies to all "substantive" laws—*i.e.*, all laws that "change and redefine the out-of-court rights, obligations, and duties of persons in their transactions with others." *Moore*, 307 S.W. 3d at 80 (citation omitted). Laws that substantively alter past transactions will not be applied retroactively without an "express" statement that the General Assembly intended such enforcement. KRS 446.080(3); *see Vinson*, 30 S.W.3d at 169 (It is "improper to apply statutory amendments [that] change[] the substantive rights and duties of litigants regarding those events which had occurred prior to the effective date.").

"This is a very fundamental principle of statutory construction in Kentucky." *Vinson*, 30 S.W.3d at 168. The presumption is a longstanding common-law doctrine that directs courts to avoid unnecessary decisions on the constitutionality of a retroactive law by requiring the legislature, in the first instance, to expressly state that it has considered the consequences of retroactive enforcement and intends for the law to be so applied. *Landgraf*, 511 U.S. at 265–68; *infra* Part I.C. Only after the legislature makes a clear and unambiguous statement of this intent will courts address the constitutional issues. *Id.* As this Court has made clear, the presumption is "*strictly construed*," "[p]articularly where a statute creates new rights or duties"—*i.e.*, where the law has a "substantive" effect on past transactions. *Hamilton v. Desparado Fuels, Inc.*, 868 S.W.2d 95, 97 (Ky. 1993) (emphasis added).

By contrast, the presumption does not affect procedural or remedial legislation—*i.e.*, laws that "apply to the in-court procedures and remedies which are used in handling pending litigation," *Vinson*, 30 S.W.3d at 169, or laws that "clarify existing law . . . or codify judicial precedent," *Moore*, 307 S.W.3d at 81. A law qualifies as remedial or procedural only if it does not impose any "new obligation[,] new duty," or new "liability" on the parties. *Benson's Inc. v. Fields*, 941 S.W.2d 473, 475–76 (Ky. 1997). As this Court has explained, it is unnecessary to apply the presumption against retroactivity to such procedural or remedial laws because they "do not . . . give past conduct or transactions new legal consequences," and therefore "*do not affect substantive rights.*" *Moore*, 307 S.W.3d at 80–81 (emphasis added) (citing *Peabody Coal Co. v. Gossett*, 819 S.W.2d 33 (Ky. 1991)).

### A. The Act is controlled by the presumption against retroactivity because the Act is substantive.

The Act is substantive because it "redefine[s]" Appellees' rights and obligations in two critical ways. First, it imposes new payment obligations and administrative costs on Appellees that conflict with their contracts. Second, it alters the statutory deadlines for Appellees' escheat of life insurance proceeds.

#### 1. The Act imposes new obligations on Appellees that conflict with their contracts.

The Act is substantive because it fundamentally alters Appellees' contractual obligations. The Act forces Appellees to make payments in circumstances not contemplated by the contracts—*i.e.*, before "due proof of death" is "received." In addition, retroactively enforcing the Act requires Appellees to incur all administrative costs necessary to regularly search for evidence of death, confirm that evidence, and locate beneficiaries for all life insurance policies issued prior to the Act's effective date. As the Court of Appeals held, "the Act shifts the burden of obtaining evidence of death and locating beneficiaries from the insured's beneficiaries and estate to the insurer." (Opinion at 9.) Requiring Appellees to establish the infrastructure necessary to perform these tasks is inconsistent with their contractual bargain, and with the premium pricing decisions they made in reliance on their contractual rights. *Supra* at 6–7.

Thus, the Act is a classic example of a "substantive" law governed by KRS 446.080(3). By placing the responsibility to establish proof of death on the insured's person's beneficiaries and estate, Appellees' contracts ensure that Appellees do not incur the costs necessary to search for evidence of death, confirm the evidence, or locate potential beneficiaries. This has kept Appellees' overhead costs low, and Appellees were

able to offer life insurance at affordable premium prices because their contracts precluded them from incurring these costs.[16]

These costs are significant. Fulfilling the Act's requirements for pre-existing life insurance policies will be time-consuming and expensive for Appellees for at least two reasons.

***First***, many of Appellees' older policies (consistent with then-existing laws) lack basic identifying information (such as Social Security numbers and addresses).[17] Without this information, a search of the DMF may result in a significant number of false positive matches—*e.g.*, an insured person with a relatively common name may "match" multiple entries on the DMF. Appellees will be forced to incur the costs necessary to investigate all of these matches and rule out the false positives, all within a 90-day window. These costs will be compounded by the undisputed inaccuracies in the DMF itself. Indeed, the authorized official provider of the DMF provides a disclaimer that "the Death Master File (DMF) may contain inaccuracies," and "it is possible for the records of a person who is not deceased to be included erroneously in the DMF."[18]

***Second***, information for Appellees' older policies generally is not stored in electronically searchable databases.[19] Thus, Appellees cannot verify DMF matches relating to many of these life insurance policies through automated processes. Rather,

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[16] Myers Decl. ¶ 12; Schallhorn Decl. ¶ 11.

[17] Myers Decl. ¶ 25.

[18] R. 21–22, Compl. ¶ 69 (quoting the initial pop-up "Disclaimer" at NTIS.gov, http://www.ntis.gov/products/ssa-dmf.aspx (last visited Dec. 11, 2015)).

[19] Myers Decl. ¶ 25.

verification will require manual review by a claims specialist, a process that is both time-consuming and expensive.[20]

***Finally***, the process of locating beneficiaries will also impose unanticipated costs on Appellees. Consistent with then-existing laws, many of Appellees' older policies lack addresses or Social Security numbers for the beneficiaries listed on the policies. Locating such beneficiaries—especially on policies issued decades ago—will be labor-intensive and costly.

Therefore, the Court of Appeals properly determined that these new statutory obligations are inconsistent with the parties' contractual agreement. The Act is substantive because it reverses the roles of the parties on the fundamental issue of who is responsible to establish proof of death.

The Court of Appeals' conclusion that this change to the contracts is substantive is not novel or controversial. Courts in other jurisdictions that have interpreted the standard "due proof of death" language in life insurance contracts' agree that the contracts "do *not* impose a duty on [insurers] to search the DMF to determine whether their insureds are deceased." *Andrews*, 2012 WL 5289946, at *6 (emphasis added). *See also Feingold v. John Hancock Life Ins.*, No. 13-10185, 2013 WL 4495126 (D. Mass. Aug. 20, 2013) (Appendix C) (insurer's "practice of holding policy proceeds until receiving proof of the insured's death" comports with state law and the terms of the "insurance policy"), *aff'd* 733 F.3d 55 (1st Cir. 2014); *Total Asset Recovery Servs., LLC v. MetLife, Inc.*, No. 2010-CA-3719, slip op. (Fla. Cir. Ct. Aug. 20, 2013) (Appendix D) (insurers are not required by their policies or state law to search for evidence of death "in

[20] *Id.*

connection with payment or escheatment of life insurance benefits"), *aff'd* No. 1D13-4420, 2014 WL 4656895 (Fla. App. Sept. 19, 2014); *Thrivent Fin. for Lutherans v. Fla. Dep't of Fin. Servs.*, 145 So. 3d 178, 180-81 (Fla. App. 2014) (Appendix E) ("[N]othing" in the contracts or state law requires insurers to "search these death records[,]" such as "the Death Master File").

The Department argues that the Act does not alter Appellees' contracts for several reasons. ***First,*** it argues that the Act does not require them to pay or escheat "'more'" than the total death benefit specified in the contract.[21] According to the Department, the Act "'merely confirms the right of beneficiaries to the money the insured's premiums have already paid for.'"[22] This ignores the fundamental question of what the contracts require to trigger the insurer's obligation to pay. Insurance underwriting is based not only on a calculation of *what* benefits are paid but also on a calculation of *when* those benefits must be paid. Appellees rely on their contracts in making those underwriting decisions. Here, the contracts expressly require payment upon "receipt" of "due proof of death." *Supra* at 3. By compelling Appellees to make payments sooner than the contracts require, the Act has "redefine[d]" Appellees' contractual rights in a substantive way. *Moore*, 307 S.W. 3d at 80.

***Second***, the Department argues that the Act does not impair Appellees' contracts because it merely requires them to obtain "notice" of death, and does not interfere with their ability to request "proof" of death—*i.e.*, a death certificate—from a claimant. (Dep't Br. at 4–5.) This is mistaken. The Act does not merely require Appellees to obtain "notice" of death—although even that would impair the contracts. Rather, the Act

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[21] Dep't Br. at 2 (quoting R.779, Circuit Court Opinion and Order at 8).

[22] *Id.* at 6 (quoting R. 779, Circuit Court Opinion and Order at 8).

requires Appellees to routinely search for evidence of death in the DMF for all policies and to "*confirm*" that evidence by obtaining and analyzing "records and information" sufficient to verify any DMF match. KRS 304.15-420(3)(a), (b)(1) (emphasis added). After that, it requires Appellees to "locate beneficiaries" and provide them "claim forms or instructions . . . to make a claim." *Id.* 304.15-420(3)(b)(2)(b). This is a substantive change.

***Third***, the Department incorrectly argues that the West Virginia Supreme Court's decision in *West Virginia ex rel. Perdue v. Nationwide Life Ins. Co.*, 777 S.E.2d 11 (2015), and the United States Supreme Court's decision *Connecticut Mutual Life Insurance Co. v. Moore*, 333 U.S. 541 (1948), indicate that the Act achieves "remedial purposes" without "impairing . . . contractual rights." (Dep't Br. at 11.) To the contrary, as further discussed below, neither case involved legislation requiring insurers to consult the DMF, and neither indicated that a law that requires insurers to search for evidence of death, confirm the evidence, and locate beneficiaries could be retroactively enforced. *Infra* at 37–39.

***Finally***, the Department argues that the Act does not "'directly alter'" a "'condition[] precedent'" to payment in the contracts.[23] Specifically, the Department points out that the Act entitles Appellees to request a death certificate from a claimant before Appellees pay a claim. KRS 304.15-420(3)(b)(2)(b). According to the Department, this is sufficient to protect Appellees' contractual rights, and the Court of Appeals decision is "internally inconsistent" for suggesting otherwise. (Dep't Br. at 1–2.)

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[23] (Dep't Br. at 2 (quoting Opinion at 9).)

There is no internal inconsistency in the Court of Appeals' decision. KRS 446.080(3)'s presumption against retroactivity applies to any law that substantively changes the "'out-of-court rights, obligations, and duties of persons in their transactions with others.'" *Moore*, 307 S.W. 3d at 80. It is immaterial whether the law "directly alters" a contractual "condition precedent." *Supra* at 14. Here, the Act "shifts the burden" of establishing evidence of death from the claimant to the insurer. (Opinion at 9.) The fact that the Act allows Appellees to request a death certificate from a claimant *after* Appellees have independently searched for evidence of death, taken steps to "confirm" that evidence, and located beneficiaries cannot mask the significance of the burden-shifting the Act imposes. The standard "receipt of due proof of death" language has been uniformly understood to provide that "the insurer has *no duty to make an independent investigation* to determine if the beneficiary is entitled to make a claim." Couch § 187:3 (emphasis added). The Act requires Appellees to conduct precisely such an investigation, nullifying the contractual agreement between the parties that the claimant will be responsible for establishing proof of death.

The fact that the Act allows Appellees to request a death certificate from a claimant *after* completing this investigation is not sufficient to preserve the substance of the contractual agreement. Appellees have bargained for the right to require the claimant to initiate the claim process and establish proof of death. The Act eliminates this right by requiring Appellees to search for and confirm proof of death, and to effectively solicit claims from beneficiaries.

In any event, Appellees' statutory right to request a death certificate after having conducted the investigation required by the Act will be redundant in most cases. Once

Appellees discover a possible match between their policy records and a DMF entry, the Act requires Appellees to obtain "records and information" to "*confirm* the death of an insured." KRS 304.15-420(3)(b)(1) (emphasis added). In many cases, the only record that can reliably confirm death *is* the death certificate.[24] Thus, according to the Department, the Act preserves the pointless "right" to demand a copy of a death certificate that Appellees almost always will have already acquired in furtherance of their efforts to satisfy the Act's requirements.

The Act unquestionably and substantively alters the contractual relationship between Appellees and their policyholders.

**2. The Act alters insurers' statutory escheat obligations.**

The Act is substantive for the independent reason that it accelerates Appellees' escheat obligations. The stated purpose of the Act is to "require recognition of the escheat statute." KRS 304.15-420(1). But, in operation, the Act does not merely "require recognition" of Kentucky's existing escheat law, it significantly expedites insurers' escheat obligations. Under existing Kentucky law, insurers must escheat life insurance proceeds within three years after (1) receipt of due proof of death (if a beneficiary is not available), or (2) the date the insured person reaches the limiting age (if proof of death is never received). KRS 393.062. By contrast, under the Act, insurers must escheat life insurance proceeds within three years of a confirmed DMF match, even if due proof of death has not been received and even if the insured person has not reached the limiting age. *Supra* at 7–8.

[24] Myers Dep. at 87:1–88:3.

Writing for the Sixth Circuit in *American Express*, Judge Siler made clear that laws that hasten escheat deadlines are "substantive," not "remedial." 730 F.3d at 632–33. In that case, the General Assembly shortened Kentucky's escheat deadline for travelers' checks from 15 to 7 years. *Id.* at 631 (citing KRS 393.062(3)). The Sixth Circuit held that this legislation was "substantive"—and therefore controlled by KRS 446.080(3)'s presumption against retroactivity—because it "clearly 'change[d] and redefine[d]'" the "'obligations and duties'" of travelers' check issuers, like American Express. *Id.* at 633 (quoting *Vinson*, 30 S.W.3d at 168). As American Express established, although most travelers' checks are cashed within a year, American Express "used the remaining uncashed [travelers' checks] for long-term, high-yield investments." *Id.* at 631. By shortening the escheat deadline, the new law shortened American Express's investment period. This reflected a "substantive" change in the legal standard for escheat. *Id.* at 632.

The only two other courts to consider this question agree. In *Biogen IDEC MA, Inc. v. Treasurer & Receiver General*, 454 Mass. 174 (2009), the Supreme Judicial Court of Massachusetts held that changes to escheat regulations cannot apply retroactively if they require the holders of property to "surrender" the property in circumstances that prior regulations did not demand. *Id.* at 191. Similarly, in *A.W. Fin. Servs., S.A. v. Empire Resources, Inc.*, 981 A.2d 1114 (2009), the Delaware Supreme Court held that legislation that "shortened" the escheat deadline for stocks from "five to three years" was "substantive," and specifically rejected the argument that the law was "remedial." *Id.* at 1119–20.

The same principle governs this case. Under the Act, Appellees must escheat unclaimed policy proceeds following a bi-annual DMF search rather than waiting until

receipt of due proof of death or the mortality limiting age. This is a substantive change in their obligations. The Department argues that the presumption against retroactivity does not apply because the Act does not impair Appellees' vested contract rights. But KRS's 446.080(3)'s presumption against retroactivity applies to *any* statute that makes a "substantive" change in the law, regardless of whether it also impairs contract rights. *See*, *e.g.*, *Vinson*, 30 S.W.3d at 169 (applying KRS 446.080(3) to substantive law that did not affect contracts). As *American Express* demonstrates, statutes that hasten escheat deadlines make a "substantive" change to *pre-existing law*, irrespective of their impact on contract rights. 730 F.3d at 632–33. American Express did not argue, and the Sixth Circuit did not find, that the escheat law in that case impaired any term of American Express's contracts. This case can be resolved on the same basis.

The Department's arguments that the Act does not "substantively" change Kentucky escheat law also fail. The Department claims that the legislation in *American Express* was substantive, and controlled by KRS 446.080(3), because it changed the "absolute maximum self-investment period" for unclaimed travelers' checks from 15 to 7 years. (Dep't Br. at 18 (emphasis omitted).) Here, the Department argues that Kentucky escheat law does not impose an absolute maximum investment period on life insurance proceeds, so "there are too many variables for the Appellees' expectancy to mature into a vested right." (*Id.*) This misses the mark. Pre-existing Kentucky law established a clear escheat deadline for life insurance: Insurers were required to escheat upon either their receipt of due proof of death or the insured person's attainment of the limiting age. *Supra* at 7–8. The Act unambiguously shortens this deadline by requiring escheat upon a confirmed DMF match, even if neither of these two conditions have been satisfied. The

General Assembly has moved the goalposts for the escheat of life insurance just as plainly as it did for travelers' checks in *American Express*.

### 3. The Act's purported "social" benefits do not render the Act remedial as the Department argues.

The Department also argues that the Act is "remedial" because the Department contends that shifting the burden to establish proof of death from the claimant to the insurer will remedy a "social" dilemma. (Dep't Br. at 1.) That misunderstands the meaning of "remedial" for purposes of the rule against retroactivity. A statute is remedial only if it merely has a procedural effect upon the remedy for a pre-existing substantive right, without changing that substantive right or creating a new substantive right. As this Court explained in *Jeffers*, "[r]emedial means no more than the expansion of an existing remedy without affecting the substantive basis, prerequisites, or circumstances giving rise to the remedy." *Kentucky Ins. Guar. Ass'n v. Jeffers*, 13 S.W.3d 606, 609 (Ky. 2000). Remedial legislation cannot change "the substantive basis, prerequisites, or circumstances giving rise" to pre-existing rights or obligations. *Id.*

This Court's precedents clearly illustrate the distinction between remedial and substantive legislation. For example, a law that changed the "causation and weight of evidence components" of a claim under the Whistleblower Protection Act was substantive, and could not be applied retroactively, because it "changed the substantive rights of employees and the obligations of employers." *Vinson*, 30 S.W.3d at 169. The Act has precisely this sort of substantive effect—it impacts insurers' contractual rights and their escheat obligations. It is not procedural.

By contrast, a law that merely changed the method by which disabled mine workers could receive statutorily-mandated "retraining incentive" payments from their

employers—by requiring the employers to pay the educational institution directly, rather than the employee—was remedial. *Thornsbury v. Aero Energy and Workers' Compensation Board*, 908 S.W.2d 109 (Ky. 1995). The law merely altered the form of the remedy without altering the substance of employees' right to the payment or employers' obligation to make it. *Id.* at 112. The Act does not have such a limited procedural effect. It fundamentally alters Appellees' contracts and significantly accelerates their escheat deadlines.[25]

The Department's views on whether retroactive enforcement of this substantive legislation would have "social" benefits are irrelevant, and misstate the intent and impact of the Act in any event. The Department claims—with no support in the Act's text or legislative history—that the Act was designed to cure an alleged unfairness in the contractual "non-forfeiture" policy provisions, which keep the policies in force after non-payment, rather than being cancelled outright. (Dep't Br. at 3–4.)

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[25] In cases such as *Jeffers*—on which the Department mistakenly relies—this Court has held that changes to the Kentucky Insurance Guaranty Association's (KIGA)'s obligations to pay an insolvent insurer's share of a worker's compensation award are "remedial" because the "KIGA is an entity created by the legislature for the protection of the public against insolvent insurers." *Benson's*, 941 S.W.2d at 476 (citing *Ky. Ins. Guar. Ass'n v. Conco, Inc.*, 882 S.W.2d 129 (Ky. App. 1994)); *Jeffers*, 13 S.W.3d at 610–11 (citing *Conco*, 882 S.W.2d 129). The General Assembly's creation of the KIGA itself was a "remedy" designed to "protect[] . . . injured workers and their employers." *Benson's*, 941 S.W.2d at 476; *Jeffers*, 13 S.W.3d at 611 ("The KIGA Act does not create a vested right. It merely provides a remedy when there is a judgment" against an insolvent insurer.") As this Court explained, changes to this public entity's responsibilities to cover an insolvent insurer's share of a worker's compensation award did "*not* involve the shifting of primary liability from one [party] to another." *Benson's*, 941 S.W.2d at 477 (emphasis added). Thus, nothing in *Jeffers* supports the retroactive enforcement of legislation, like the Act, that retroactively alters private parties' contracts and escheat obligations.

This severely misrepresents the purpose of these non-forfeiture provisions, and the reasons they have been added to Appellees' life insurance policies. The General Assembly has *required* Appellees and other insurers to include these non-forfeiture provisions in their policies. KRS 304.15-310 ("No policy of life insurance . . . shall be delivered or issued for delivery in this state unless it shall contain . . . (a) Paid up non-forfeiture benefit."). Kentucky, like many other states, requires non-forfeiture provisions as a matter of consumer protection. *See, e.g., Couch* § 77:28 (Non-forfeiture provisions are "designed for the benefit of the insured."). In the absence of non-forfeiture provisions, if a policyholder failed to make a single payment, the policy would lapse, eliminating the policyholder's right to *any* benefit. Non-forfeiture provisions prevent this result by requiring the insurer to use the policy's accumulated cash value to either (a) purchase a term policy at the same face value,[26] or (b) purchase a paid-up whole life benefit for the policyholder at a lower face amount than the original policy provided.[27] In either case, the non-forfeiture provision assists the policyholder by providing the same benefit for a longer period of time post-lapse or providing a reduced benefit after lapse.

In fact, the Department has approved all of Appellees' policy forms containing non-forfeiture provisions. *Supra* at 4; KRS 304.14-120. When the "Kentucky insurance commissioner approved [an insurer's] policy form, we assume he necessarily found that its [non-forfeiture] provisions are at least as favorable to the . . . policyholder as the minimum requirements specified under KRS 304.15-310 [the non-forfeiture statute]." *Liberty Nat'l Bank & Trust Co v. Life Ins. Co of Cincinnati*, 90 F.2d 539, 548 (6th Cir. 1990). Thus, what the Department describes as a "scheme," (Dep't Br. at 3.), is in fact a

[26] The Department refers to this as "extended term insurance." (Dep't Br. at 3.)

[27] The Department refers to this as "reduced paid-up" insurance. (*Id.* at 3 n.11.)

consumer-protection provision required by the General Assembly and approved by the Department itself.

Significantly, the Act does not amend these consumer protection statutes in any way. If the General Assembly perceived some "social" wrong in the non-forfeiture statute, KRS 304.15-310, then it should have directly amended that statutory framework. Instead the Act exclusively addresses—and alters—insurers' obligations to pay and escheat proceeds for *deceased* insureds. Non-forfeiture provisions do not apply to deceased insureds. They apply only when the policy owner is still alive, but has ceased paying premiums. The Act's change to the substantive procedures for making a claim when an insured has died has nothing to do with non-forfeiture provisions, which solely address the cash surrender value of a policy when the policy owner is still living, but has stopped making payments.[28]

Moreover, despite its speculation about the Act's purported "social" benefits, the Department fails to acknowledge that the Act's expressed purpose is to "require recognition of the escheat statute" and that the Act's effect is to significantly accelerate the Commonwealth's receipt of revenue for unclaimed life insurance policies. KRS 304.15-420(1), (5); *supra* at 7–8, 21. The Court of Appeals' holding that such a law is substantive follows directly from the Sixth Circuit's *American Express* decision and this Court's precedents.

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[28] The Department—citing a recent West Virginia Supreme Court decision—also argues that retroactive enforcement of the Act is necessary to prevent insurers from asymmetrically relying on the DMF, a practice in which an insurer consults the database to terminate "'annuity contract[s],'" but fails to consult the database for evidence of deceased insureds. (Dep't Br. at 11 (quoting *Perdue*, 777 S.E.2d at 14–15).) Whatever the merits of that policy argument, it is for the General Assembly to consider in the first instance. *Infra* Part I.C. Moreover, the argument has no relevance to Appellees—they do not sell annuities.

### B. The Act lacks an express statement of retroactive intent.

After determining that the Act is substantive, the Court of Appeals properly held that KRS 446.080(3) precludes its retroactive enforcement because the Act lacks an "express" statement of any such intent. The Act simply states that "[a]n insurer shall perform a comparison of its insureds' in-force life insurance policies . . . against a Death Master File, on at least a semi-annual basis" and shall then follow the additional required steps. KRS 304.15-420(3). The Act is silent as to whether it applies to *all* policies in force in the Commonwealth, including those that pre-date its enactment, or only to those policies entered into force after it became effective. That legislative silence should end the inquiry. *See Hamilton*, 868 S.W.2d at 97 (KRS 446.080(3)'s presumption against retroactivity must be "strictly construed"); *Am. Express*, 730 F.3d at 633 (applying KRS 446.080(3)'s presumption because statute did "not expressly declare that the change was meant to be applied retroactively").

Indeed, it is especially appropriate to apply the presumption against retroactivity to the Act because in this case—as in *American Express*—the General Assembly amended the Act during the pendency of the litigation, but declined to clarify its intent regarding retroactive enforcement. *Infra* at 10. As Judge Siler explained for the Sixth Circuit in *American Express*, "the legislature knew how to express retroactivity" in this statute. 730 F.3d at 633. The fact that the legislature <u>twice</u> "declined the opportunity" to do so—once upon adopting the statute, and once upon amending it—provides ample reason to hold that the Act has no retroactive sweep. *Id.*

Inferring retroactive intent from legislative silence is particularly inappropriate in this case because other state legislatures that have expressly considered whether similar legislation should apply retroactively have consistently decided *against* such

enforcement. As noted, 19 states, including Kentucky, have adopted versions of the NCOIL model law on which the Act is based. *Supra* at 5. Legislatures in five of those states have expressly declared that their laws do *not* apply retroactively.[29] Legislatures in four other states have declared that their laws apply retroactively only in limited circumstances—against insurers that previously used the DMF "asymmetrically" to terminate payments on annuities, but not to search for evidence of death on life insurance policies.[30] (Appellees are not in this category because they do not sell annuities.) *No* state legislature has expressly made this legislation retroactive as to all insurers. The nine remaining states, like Kentucky, have enacted statutes that are silent on the point.[31]

Moreover, the trend among legislatures that have considered the issue most recently has been strongly *against* retroactive enforcement. While states, like Kentucky, that adopted versions of the model law in 2012 and 2013 often did not state a position on retroactive or prospective enforcement, seven of the ten states that have adopted such legislation in the last two years have expressly restricted its retroactive use.[32]

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[29] *See* Ala. Code § 27-15-51(b); 2015 Ark. Laws Act 905 (S.B. 768) § 2; Ga. Code § 33-25-14; Ind. Code §§ 27-2-23-9(a), 27-2-23-11; S.B. 2796 § 4(3), 2014 Leg., Reg. Sess. (Miss. 2014).

[30] *See* N.M. Stat. Ann. § 59A-16-7.1(F); N.C. Gen. Stat. § 58-58-390(b)(2)(a); Tenn. Code § 56-7-3404(a)(3); Utah Code Ann. § 31A-22-1903(2)(a).

[31] Idaho Code Ann. § 41-3002; Iowa Code § 507B.4C; Md. Code, Ins. § 16-118; Mont. Code § 33-20-1604; Nev. Rev. Stat. § 688D.010 to .140; N.Y. Ins. Law § 3240; N.D. Cent. Code § 26.1-55-01; R.I. Gen. Laws § 27-80-4; Vt. Stat. Ann. Tit. 27, § 1244a.

[32] Arkansas, Georgia, Indiana, and Mississippi all adopted laws that are expressly prospective. *Supra* n.29. North Carolina, Tennessee, and Utah all adopted laws that do not apply retroactively unless the insurer used the DMF asymmetrically. *Supra* n.30. Idaho, Iowa, and Rhode Island adopted laws that do not expressly state a position on retroactive or prospective enforcement. *Supra* n.31.

### C. The Court of Appeals' narrow decision is deferential to the legislature.

The Court of Appeals' holding was narrow. By resolving this case on statutory grounds, the Court avoided Appellees' constitutional arguments. That is the outcome KRS 446.080(3) is designed to produce.

It is well-established that retroactive enforcement of new laws raises serious constitutional questions. *See Landgraf*, 511 U.S. at 266 ("[T]he antiretroactivity principle finds expression in several provisions" of the United States "Constitution," including the Contract Clause.) In addition, even if the Constitution is not violated, "[r]etroactive legislation presents problems of unfairness" because it "can deprive citizens of legitimate expectations and upset settled transactions." *Gen. Motors Corp. v. Romein*, 503 U.S. 181, 191 (1992). By refusing to apply statutes retroactively without an express statement of such intent from the legislature, courts avoid prematurely adjudicating constitutional questions that the legislature has not expressly put at issue. As the United States Supreme Court has explained, this "requirement that Congress first make its intention clear helps to ensure that Congress *itself* has determined that the benefits of retroactivity outweigh the potential for disruption or unfairness." *Landgraf*, 511 U.S. at 268 (emphasis added).

This policy of judicial restraint and deference to the legislature supports the separation of powers. *See* Ky. Const. §§ 27, 28. Indeed, as a general matter, when interpreting a statute, "[i]t is neither the duty nor the prerogative of the judiciary to breathe into the statute that which the Legislature has not put there." *Virgin Mobile USA, LP v. Commonwealth ex rel. Commercial Mobile Radio Serv. Telecomms. Bd.*, 448 S.W.3d 241, 249 (Ky. 2014) (internal quotation marks omitted). On the issue of

retroactivity in particular, KRS 446.080(3) makes clear that the General Assembly wishes to speak "expressly" before a court interprets a statute as retroactive and then prematurely decides the constitutional question. Kentucky courts "strictly construe[]" KRS 446.080(3)'s presumption against retroactivity to ensure that the General Assembly retains its longstanding prerogative to address these issues in the first instance. *See Hamilton*, 868 S.W.2d at 97; *Landgraf*, 511 U.S. at 268. There is no reason to deviate from that approach in this case.

Another time-honored canon of construction—the doctrine of constitutional avoidance—supports the same conclusion. It is a "long-observed principle that Constitutional adjudication should be avoided unless strictly necessary for a decision in the case." *Spees v. Ky. Legal Aid*, 274 S.W.3d 447, 449 (Ky. 2009). Indeed, the presumption against retroactivity is a natural extension of this doctrine. *See, e.g., Ward v. Dixie Nat'l Life Ins. Co.*, 595 F.3d 165, 177 (4th Cir. 2010) (recognizing that the "presumption against retroactivity" and the "doctrine of constitutional avoidance" are both "premised on the 'reasonable' notion that legislatures 'd[o] not intend [an interpretation] which raises serious constitutional doubts'" (alterations in original) (quoting *Clark v. Martinez*, 543 U.S. 371, 382 (2005))); *Kia Motors Am., Inc. v. Glassman Oldsmobile Saab Hyundai, Inc.*, 706 F.3d 733, 740 (6th Cir. 2013) (applying presumption against retroactivity as a means to avoid "a significant constitutional question"). KRS 446.080(3) provides an avenue to avoid the constitutional questions here. This Court need not decide whether retroactive enforcement of the Act is constitutional if the Court determines that the Act does not apply retroactively at all.

The Department urges this Court to "presume" that the Act's retroactive enforcement is constitutional because, it says, this Court's "awesome" power to strike down unconstitutional legislation should be used sparingly. (Dep't Br. at 8.) This approach would turn the doctrine of constitutional avoidance on its head. The proper approach, dictated by this Court's precedents, is to *avoid* the constitutional questions by interpreting the statute in a way that avoids confronting the constitutional question. *Am. Trucking Ass'n v. Commonwealth, Transp. Cab.*, 676 S.W.2d 785, 789–90 (Ky. 1984). The Court of Appeals appropriately followed that precedent.

Finally, the Court of Appeals' ruling is fully consistent with a long line of precedents from across the country, in which courts have been especially vigilant in applying the presumption against retroactivity to laws that impair insurance contracts. As the United States Supreme Court has held, the presumption should be applied with particular rigor whenever a new law impairs "legitimate expectations" in relationships in which "predictability and stability" are important. *Romein*, 503 U.S. at 191; *Landgraf*, 511 U.S. at 271. No industry better embodies the value of "predictability and stability" than the life insurance industry. Contracts for whole life insurance, by definition, last for the lifetime of the insured and cannot be renegotiated. The financial stability of the life insurance industry—and insurers' concomitant ability to pay the promised benefits—rests upon insurers' "painstaking assessment of the[ir] likely liability" and their establishment of corresponding premium rates that will be "adequate" to meet the demands of such claims in future years. *Allied Structural Steel*, 438 U.S. at 246.

"Drastic changes" in the law that affect insurance contracts, and premiums developed in reliance on those contracts, can "jeopardize[] the insurer's solvency and,

ultimately, the insureds' benefits." *Id.* at 247. Thus, courts have demanded a clear and express statement from the legislature before applying such changes retroactively. *See, e.g., Sparks v. Craft*, 75 F.3d 257, 262 (6th Cir. 1996) (refusing to retroactively apply a Kentucky statute requiring insurers to make available certain coverage for underinsured motorists); *Allstate Ins. Co. v. Boston Whaler, Inc.*, 510 N.E. 2d 1180, 1182 (Ill. App. Ct. 1987) (Laws should not be enforced retroactively when they "create a new financial obligation for the insurer that was not part of the original agreement"); *Rudolph v. Weckesser*, 675 So. 2d 1158, 1160 (La. Ct. App. 1996) (same); *Burnham v. Bankers Life & Cas. Co.*, 470 P.2d 261, 264 (Utah 1970) (same); *Higgins v. MFA Mut. Ins. Co.*, 550 S.W.2d 811, 814 (Mo. Ct. App. 1977) (same).

## II. If applied retroactively, the Act violates the Contract Clauses of the Kentucky and United States Constitutions.

In the event this Court does not resolve this case on statutory grounds by presuming that the Act applies only prospectively, the Court should hold that the Act's retroactive enforcement against Appellees' pre-existing life insurance policies violates the Contract Clause of the Kentucky and United States Constitutions. The test for whether a statute violates the Contract Clause consists of essentially the same two-step inquiry under both Kentucky and federal law. *See Union Trust, Inc. v. Brown*, 757 S.W.2d 218, 210-20 (Ky. App. 1988). At the first step, the court asks whether the law has "operated as a substantial impairment of a contractual relationship." *Gen. Motors Corp.*, 503 U.S. at 186. At the second step, a law causing a substantial impairment may be upheld only if it serves a "significant" public purpose, *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, 459 U.S. 400, 412 (1983), and is an "appropriately tailored" means of achieving that purpose, *Allied Structural Steel*, 438 U.S. at 242.

### A. The Act substantially impairs Appellees' contract rights.

Retroactively enforcing the Act against Appellees' pre-existing life insurance policies violates the first step of the Contract Clause test because it "shifts the burden" of establishing death from claimants to insurers, in conflict with Appellees' contractual right to await "receipt" of "due proof of death" before taking steps to investigate and pay claims. (Opinion at 9.) As the United States Supreme Court has explained, "in any bilateral contract the diminution of duties on one side effectively increases the duties on the other." *Allied Structural Steel*, 438 U.S. at 244 n.16. The Act has just this sort of impact.

Indeed, the Act impairs Appellees' pre-existing contracts in a manner similar to the one caused by a Minnesota statute that the United States Supreme Court held unconstitutional in *Allied Structural Steel*. That statute retroactively "change[d]" an employer's pension-funding obligations in contracts with its employees, to the extent that the employer's "past contributions [to the pension fund] were adequate when made" but "not adequate when computed under the [new] statutory vesting requirement." *Allied Structural Steel*, 438 U.S. at 246. The Supreme Court held that the statute substantially impaired the employer's contracts because the employer's reliance on the funding requirements of the pensions was vital to its agreement to enter those contracts, and the statute imposed obligations on the employer "conspicuously beyond those it voluntarily agreed to undertake." *Id.* at 240.

The Act has the same effect. Appellees never "agreed" to the new obligations it imposes, which strip away their contractual right to investigate and settle claims only for those policies for which they have received due proof of death. This contractual right preserved Appellees' ability to avoid the administrative costs necessary to regularly

search for proof of death, confirm the proof, and locate beneficiaries. *Supra* at 6–7, 15–17. It also preserved their ability to retain and invest life insurance proceeds until either they received "due proof of death" or the insured reached the "limiting age." *Id.* Courts have recognized that laws that deprive parties of such contractual interests raise constitutional problems. For example, in *New Jersey Retail Merchants Association v. Sidamon-Eristoff*, 669 F.3d 374 (3d Cir. 2012), the Third Circuit preliminarily enjoined the retroactive enforcement of a New Jersey escheat law that shortened the investment period for stored-value cards, holding that it likely violated the Contract Clause because it interfered with merchants' "expected benefits" under their pre-existing contracts with stored-value card recipients. *Id.* at 387. Similarly, in *United Healthcare Ins. Co v. Davis*, 602 F.3d 618 (5th Cir. 2010), the Fifth Circuit held that a statute that retroactively altered health insurance policies violated the Contract Clause because it "offset" insurers' "expected returns from the contracts in a way that was not foreseeable when the contracts began." *Id.* at 630. The Act has the same impact, and each of the Department's attempts to minimize the severity of this impairment are unavailing.

***First***, the Department argues that Appellees' contractual rights are too speculative to warrant protection. According to the Department, Appellees do not have a "guarantee as to how long they would have custody of the funds or what benefit they would receive from them" because claimants can furnish Appellees with proof of death at any time (Dep't Br. at 18.) This misunderstands the right Appellees have bargained for. Under the contracts, Appellees have the right to the proceeds on *all* policies until the insured reaches the limiting age, unless Appellees receive "due proof of death" from a claimant sooner. This is a fully enforceable contractual interest. Just as a person who contracts for

a life estate in land has no "guarantee" of how long he or she will live and thereby retain possession, that person nonetheless has a perfectly valid and enforceable right to hold the land until the condition precedent occurs. Appellees have precisely the same type of contractual right here.

***Second***, the Department mistakenly conflates Appellees' assertion of their legitimate and enforceable contractual rights, which the Contract Clause protects, with a generalized expectation in the enforcement of existing law, which it does not. The Department argues that Appellees have no more right to expect that the legislature would not disturb longstanding industry practice than a taxpayer has in preserving the "Internal Revenue Code" as written. (Dep't Br. at 19.) But the Department ignores fundamental distinctions between those two situations. Appellees' right to condition their investigation and payment of claims on receipt of due proof of death is set forth *in a contract*; a generalized expectation that the legislature will not change the Internal Revenue Code is not a contractual right. The precedents the Department cites merely stand for the principle that the legislature generally has authority to change the law.[33] None endorse the argument that the legislature may retroactively change contracts without any constitutional restraint. Moreover, none involve KRS 446.080(3), which

[33] In *United States v. Carlton*, 512 U.S. 26 (1994), taxpayers challenged a statute altering a tax deduction, and the Court merely rejected the argument that they had a due process right to retain the deduction offered by prior law. *Id.* at 34–35. No contractual rights were at stake. In *King v. Campbell County*, 217 S.W.3d. 862 (Ky. 2006), taxpayers claimed the right to resist another change in the tax code. No contractual rights were at stake. *Id.* Finally, in *Louisville Shopping Ctr., Inc. v. City of St. Matthews*, 635 S.W.2d 307 (Ky. 1982), property owners challenged a law altering annexation procedures for commercially developed parcels of land; again, no contractual rights were at stake. *Id.* at 308.

prevents the retroactive enforcement of statutes that substantively change the law, without regard to whether contract rights are at stake. *Supra* at 23.

***Third***, the Department argues that any impairment of Appellees' contracts is minor. According to the Department, Appellees already engage in a "good faith" effort to pay claims when they are notified of an insured's death by someone other than the claimant—typically, a funeral director.[34] (Dep't Br. at 1, 5.) That misunderstands the record. The fact that Appellees *voluntarily* take steps to verify a potential death for those few policies where they are contacted by a funeral director rather than the beneficiary does not support the conclusion that a law *mandating* Appellees to undertake systematic and expensive efforts to search electronic databases and take other steps to confirm deaths on *all* policies imposes no change on their contracts.

***Finally***, the Department argues that two precedents settle the question, but both address very different laws than those at issue here. The Department argues that the West Virginia Supreme Court's decision in *Perdue* shows that the Act achieves "remedial purposes" without "impairing . . . contractual rights." (Dep't Br. at 11.) The Court in *Perdue* made no such finding. Neither the Contract Clause, the presumption against retroactivity, nor any statute requiring DMF searches was at issue in that case. Rather, the Court simply held that West Virginia's existing unclaimed property law, as adopted in 1997, requires insurers to escheat life insurance proceeds three years after the insured's death, rather than three years after receipt of due proof of death. *Perdue*, 777 S.E.2d 11; *see* W. Va. Code §§ 36-8-1(13)(vi), 36-8-2(a)(8), 36-8-2(e). The Court never addressed whether retroactive enforcement of a new law comparable to the Act would be

[34] *See* Schallhorn Dep. at 24:2–23, 38:1–39:3; Myers Dep. at 32:20–23.

constitutional. In fact, the Court expressly held that West Virginia law did *not* require insurers to search the DMF. 777 S.E.2d at 19.[35]

The Department also errs in relying on the United States Supreme Court's decision in *Connecticut Mutual*. In that case, the Supreme Court addressed a challenge to a New York statute that required insurers to escheat life insurance proceeds within seven years after either (a) the insured reached the limiting age, or (b) the insured had died. 333 U.S. 541. The Court acknowledged that these requirements impaired the contracts (because they required escheat even if the insurer had not received a certified death certificate), but held that the impairment was not sufficiently great to violate the Contract Clause. *Id.* The Court *never* suggested that a law comparable to the Act could withstand constitutional scrutiny.

Indeed, the contractual impairment in *Connecticut Mutual* was far more limited than what the Act's retroactive enforcement would require. The New York statute in *Connecticut Mutual* did not require insurers to take affirmative steps—or incur the necessary costs—to search for evidence of death, confirm the evidence, or locate

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[35] Moreover, the Court's holding in *Perdue* was an outlier. In concluding that West Virginia law required the escheat of life insurance proceeds upon the insured's death, rather than the insurer's receipt of due proof of death, the Court relied on a provision of West Virginia's escheat statute that has no comparable analogue in Kentucky law. *Perdue*, 777 S.E.2d at 16–17; *see* W. Va. Code § 36-8-2(e) (stating that property in West Virginia can be escheatable even if the owner "fail[s] to make demand or present an instrument or document otherwise required to obtain payment"). Appellees' submit that this analysis was erroneous. Other provisions of West Virginia escheat and insurance law expressly indicate that life insurance proceeds are not escheatable until they become "due and payable" under the contractual terms of the life insurance policy, or until the insured reaches the limiting age. W.Va. Code §§ 36-8-1(13)(vi), 36-8-2(a)(8). Regardless, *every other jurisdiction* to consider the question has held that life insurance proceeds are *not* escheatable upon the insured person's death, but only upon the insurer's receipt of due proof of death or the insured person's attainment of the limiting age. *See supra* at 17–18 (collecting authorities). *Perdue*'s analysis of West Virginia law simply has no bearing on the questions presented here.

beneficiaries. It simply required the insurer to escheat at the limiting age or after the insured had died. Insurers can determine whether an insured person has reached the limiting age through straightforward arithmetic; no DMF searches or costly verification protocols are required. Similarly, the Supreme Court construed the provision of the New York statute calling for escheat upon the insured's death narrowly—*i.e.*, only to require escheat when the insurer already *knew* the insured had died. 333 U.S. at 545–47. There was never any suggestion that the New York law required insurers to adopt an affirmative program to regularly search for and confirm evidence of death for all policies, or locate beneficiaries.

These burdens, which the Act retroactively imposes on Appellees, are far greater than those at issue in *Connecticut Mutual*. The Supreme Court's decision to uphold the New York statute's limited requirements does *not* suggest that the Act can fundamentally restructure Appellees' constitutional rights and obligations retroactively.

### B. Retroactively enforcing the Act is not an appropriately tailored means of achieving any legitimate state interest.

The Act's substantial impairment of Appellees' contractual rights can be justified only if the Act's retroactive enforcement is a "narrow" and "reasonable" measure designed to remedy an "emergency need," *Allied Structural Steel*, 438 U.S. at 242, or a "broad and general social or economic problem," *Energy Reserves Group*, 459 U.S. at 411–12. It is not.

Courts use a sliding scale when examining whether a public need is sufficiently important to allow a contractual impairment: "The severity of the impairment measures the height of the hurdle the state legislation must clear." *Allied Structural Steel*, 438 U.S. at 245. If the impairment is minor, an important public purpose may allow it. *Id.* Here,

however, the impairment is severe—the Act completely eliminates a core provision of Appellees' contracts and thereby dramatically restructures the parties' rights and responsibilities. This type of fundamental impairment can only be warranted by the most urgent public need. *Id.*

The Act's objectives fall short of that mark. The Act's stated purpose is to "require recognition of the escheat statute" and to "require complete and proper disclosure, transparency, and accountability relating to any method of payment for life insurance benefits." K.R.S. 304.15-420(1). These objectives—though legitimate—are not addressing the type of urgent public crises courts have required to justify a contractual impairment as significant as the one at issue here. *See, e.g., State v. All Prop. & Cas. Ins. Carriers*, 937 So. 2d 313 (La. 2006) (upholding law modifying contracts to provide homeowners extra year to file claims following Hurricanes Katrina and Rita); *Home Bldg. & Loan Assn. v. Blaisdell*, 290 U.S. 398 (1934) (upholding law modifying contracts to provide emergency foreclosure relief during Great Depression).

Moreover, the Act's objectives can be accomplished through alternative means that do not impair contractual rights. For example, the General Assembly could increase the penalties for violating the escheat laws Kentucky already has on the books.

In addition, to the extent the General Assembly is concerned about beneficiaries who cannot locate information about a policy or the insurer that issued it, Kentucky could adopt a "lost policy locator" program—used in at least 14 other states—in which potential beneficiaries of a deceased person are entitled to report a death to the state insurance department, and the department furnishes the information to all licensed

insurers in the state, enabling the claim to be processed.[36] Importantly, states that operate these programs typically require the potential beneficiary to submit a death certificate with this request, along with other vital information regarding the deceased person.[37] This enables insurers to promptly review their records to determine whether they have issued a policy covering the deceased person. Moreover, this ensures that the claimant—the person in the best position to know of the insured's death and to obtain a death certificate—retains the responsibility to initiate the claim process. These programs serve the public interest by assisting beneficiaries in obtaining lost policy information without impairing contract rights or the fundamental economic terms underlying the life insurance policy.

Finally, the Act would substantially achieve its goals even if it were applied only on a prospective basis. This would enable insurers to modify their policies and premiums to account for the new obligations the General Assembly has decided to impose.

The Department offered no evidence why retroactive application, and a severe contractual impairment, is necessary to achieve the Act's limited goals. As the state actor

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[36] *See* American Council of Life Insurers, Life Insurance: State Resources, https://www.acli.com/Consumers/Life%20Insurance/Pages/Missing%20Policy%20Tips.aspx (providing links to lost life insurance policy search services operated by the Departments of Insurance in Alabama, Kansas, Louisiana, Missouri, New York, North Carolina, Ohio, Oklahoma, Oregon, Texas, and Vermont, and providing information regarding programs in Massachusetts, Pennsylvania, Rhode Island, and Puerto Rico, which "provide policy locator services by request").

[37] *See*, *e.g.*, Louisiana Department of Insurance Life Insurance Policy Search Form (https://www.ldi.la.gov/onlineservices/LifeInsPolicySearch/) ("Your request cannot be handled without a copy of the death certificate."); North Carolina Department of Insurance Lost Life Insurance Policy Locator Form (http://www.ncdoi.com/Consumer/Documents/Lost%20Life%20Insurance%20Policy%20Locator%20(Print).pdf) ("Attach an original death certificate."); Oklahoma Department of Insurance Life Policy Locator Service Form (requiring certification that requestor has "provided a copy of the death certificate of the deceased").

seeking summary judgment to defeat Appellees' Contract Clause claim, the Department bears that burden. *See HealthNow New York Inc. v. N.Y. State Ins. Dep't*, 110 A.D.3d 1216, 1220 (N.Y. App. Div. 2013) (state actor must demonstrate *both* a "legitimate public purpose" served by the legislation *and* "demonstrate that retroactive application of the [legislation] [i]s a reasonable and appropriate means by which to achieve this objective").

The Department overlooks these fundamental points. Appellees' right to condition the investigation and payment of claims on their "receipt" of "due proof of death" is a central provision of their life insurance policies. Eliminating that right substantially impairs those contracts, and none of the Department's proffered objectives warrant such a dramatic intrusion.

The Department misstates the Act's purpose and practical effect by arguing that it is necessary to the "public interest" because it "ensure[s] that Kentucky consumers get what they pay for." (Dep't Br. at 19.) Kentucky policyholders that have purchased life insurance from Appellees have "paid for" the right to obtain life insurance proceeds upon the insurer's "receipt" of "due proof of death," not under the different standards imposed by the Act. The Act is not necessary to enforce the parties' existing bargain; rather, it fundamentally changes their contractual arrangement.

Moreover, the Act's effect is not merely to require the payment of life insurance proceeds to beneficiaries, it is to accelerate Appellees' obligations to escheat those proceeds to the State. In the many cases in which the Act compels a payment, but a beneficiary cannot be located, the State—*not* the beneficiaries of the insured—will receive the funds. As courts have recognized when evaluating legislation that accelerates escheat requirements, "'complete deference'" to the State's "'assessment'' of such an

Act's "'reasonableness and necessity is *not appropriate*'" because "'the State's self-interest is at stake.'" *Sidamon-Eristoff*, 669 F.3d at 388 (emphasis added) (quoting *U.S. Trust Co. of New York v. New Jersey*, 431 U.S. 1, 26 (1977) (issuing preliminary injunction against legislation altering escheat deadlines on grounds that it likely violated the Contract Clause).

The Department's "public interest" arguments are subject to the same heightened scrutiny here. The Act's retroactive enforcement against Appellees' preexisting life insurance policies is unconstitutional.

## CONCLUSION

Based on the foregoing, the Court of Appeals' decision should be **AFFIRMED**.

Dated: December 11, 2015

Respectfully submitted,

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